

**UNITED STATES OF AMERICA  
BEFORE THE  
FEDERAL ENERGY REGULATORY COMMISSION**

<b>Alliance Companies</b>	)	
	)	
<b>Ameren Corporation</b>	)	
<b>On behalf of:</b>	)	
<b>Union Electric Company</b>	)	
<b>Central Illinois Public Service Company</b>	)	
	)	
<b>American Electric Power Service Corporation</b>	)	<b>Docket Nos. RT01-88-005,</b>
	)	<b>ER99-3144-013, and</b>
	)	<b>EC99-80-013</b>
<b>On behalf of :</b>	)	
<b>Appalachian Power Company</b>	)	
<b>Columbus Southern Power Company</b>	)	
<b>Indiana Michigan Power Company</b>	)	
<b>Kentucky Power Company</b>	)	
<b>Kingsport Power Company</b>	)	
<b>Ohio Power Company</b>	)	
<b>Wheeling Power Company</b>	)	
	)	
<b>Consumers Energy Company</b>	)	
<b>and Michigan Electric Transmission Company</b>	)	
	)	
<b>The Dayton Power and Light Company</b>	)	
	)	
<b>The Detroit Edison Company</b>	)	
<b>and International Transmission Company</b>	)	
	)	
<b>Exelon Corporation</b>	)	
<b>On behalf of:</b>	)	
<b>Commonwealth Edison Company</b>	)	
<b>Commonwealth Edison Company</b>	)	
<b>of Indiana, Inc.</b>	)	
	)	
<b>First Energy Corporation</b>	)	
<b>On behalf of:</b>	)	
<b>American Transmission Systems, Inc.</b>	)	
<b>The Cleveland Electric Illuminating</b>	)	
<b>Company</b>	)	
<b>Ohio Edison Company</b>	)	
<b>Pennsylvania Power Company</b>	)	
<b>The Toledo Edison Company</b>	)	
	)	
<b>Illinois Power Company</b>	)	
	)	
<b>Northern Indiana Public Service Company</b>	)	
	)	
<b>Virginia Electric and Power Company</b>	)	

**JOINT COMMENTS OF THE**  
**ILLINOIS COMMERCE COMMISSION, MICHIGAN PUBLIC SERVICE**  
**COMMISSION, AND THE PUBLIC UTILITIES COMMISSION OF OHIO**

Pursuant to Rule 211 of the Commission's Rules of Practice and Procedure, 18 C.F.R. §385.211, the Illinois Commerce Commission, the Michigan Public Service Commission, and the Public Utilities Commission of Ohio (collectively "Midwest State Commissions") hereby submit their Joint Comments on the filing submitted by the Alliance Companies in the above-captioned dockets on August 27, 2001, which constitutes the Alliance Companies' proposed business plan for establishing the independence of the Alliance RTO ("August 27 Filing"). The Midwest State Commissions respectfully request that the Commission: (1) reject the limited scope of authority for the trustees in the interim governance proposal contained in the Alliance Companies' August 27 Filing; (2) direct the Alliance Companies to comply with the Commission's orders concerning interim independent decision-making; (3) require the Alliance Companies to bear the consequences of their failure to previously comply with the Commission's independence requirements; (4) direct the Alliance Companies to implement a permanent governance structure that comports with the Commission's RTO independence requirements; (5) reject all provisions in the term sheet which might interfere with National Grid's or Alliance LLC's independence from the Alliance Companies; (6) require the term sheet be amended to include "call" rights for the Alliance LLC that mirror the Alliance Companies' "put" rights; and (7) defer ruling on any term sheet provisions involving a Non-Divesting Transmission Owner (NTDO) advisory committee until after the advisory committee issue is resolved in the Alliance Companies' separate compliance docket.

## **I. BACKGROUND**

On January 16, 2001, the Alliance Companies submitted a filing in compliance with Order No. 2000 (“Initial Order No. 2000 Compliance Filing”) to implement the proposed Alliance RTO. The Alliance Companies proposed that independence of Alliance RTO would be established through one of two business approaches. The Alliance Companies noted that they were pursuing the possibility of attracting a strategic investor, i.e., a non-market participant that has experience and expertise in transmission or a related business, to make an equity investment in and to become the managing member of Alliance Transco. Alternatively, the Alliance Companies proposed to identify financial-only investors, i.e., investors who do not possess operational experience in the electric transmission or related business. The Alliance Companies have had full control of the RTO development and filing process from the outset and continue to do so. Since their January filing, the Alliance Companies have had ample opportunity to develop a revised governance and decision-making structure, obtain the subsequent Commission approval and seat an independent board to supervise the RTO development and start-up process.

After many months of inaction on the issue of interim governance and decision-making independence by the Alliance Companies, the Commission issued an Order on July 12, 2001, directing the Alliance Companies to establish an independent board “from the date of [the] Order.”<sup>1</sup> The Commission’s July 12 Order found that either of the two proposals submitted by the Alliance Companies in their Order No. 2000 compliance filing for achieving independence of the Alliance Transco can satisfy the requirements of Order No. 2000, provided the investors are not market participants and provided that no market participant controls Alliance Transco.

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<sup>1</sup> July 12, 2001 “Order on RTO Filing” in the Alliance dockets, 96 FERC ¶ 61,052 (2001) (“July 12 Alliance Order”).

Despite the Commission's directive, the Alliance Companies did not take steps that would immediately establish an independent board or independent decision-making. In response to the Alliance Companies' inaction, five state commissions ("State Commissions") filed a Motion for Clarification and Request for Expedited Action in these dockets on August 8, 2001 ("August 8 Motion").<sup>2</sup> The State Commissions specifically requested that the Commission order the Alliance Companies to begin the Board selection process immediately and to have the process completed on or before August 15, 2001. The State Commissions also requested that stakeholders be allowed to participate in the Board selection process, similar to what the Commission has required in other RTO cases.<sup>3</sup>

In addition to the filing of the August 8 Motion, the State Commissions and stakeholders concerned about the independence of the Alliance RTO have made a good faith effort to resolve the governance and decision-making independence issue with the Alliance Companies on an informal basis. Eight state commissions formally requested the assistance of the Commission's Office of Dispute Resolution ("ODR") to resolve issues related to the development and implementation of an appropriate Alliance stakeholders' advisory process.<sup>4</sup> In letters dated July 30, 2001, and July 31, 2001, the state commissions explained that the stakeholder advisory

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<sup>2</sup> "Motion for Clarification and Request for Expedited Action, or in the Alternative, Request for Rehearing of the Virginia State Corporation Commission, Illinois Commerce Commission, Indiana Utility Regulatory Commission, Michigan Public Service Commission, and West Virginia Public Service Commission," filed August 8, 2001.

<sup>3</sup> *GridFlorida LLC*, 94 FERC ¶ 61,020, p. 61,046 (2001); *Carolina Power & Light Co., et al.*, 94 FERC ¶ 61,273, p. 61,988 (2001).

<sup>4</sup> In so doing, they were following the suggestion of the Commission itself set out in the July 12 Order ("Therefore, we reiterate that if the parties cannot develop an acceptable stakeholder process, the Commission will step in. To aid the parties in this endeavor, we are making available the Commission's Office of Dispute Resolution."). July 12

Order, 96 FERC at 61,146. See Letter to Richard L. Miles from Jennifer M. Granholm, Attorney General, State of Michigan, the Michigan Public Service Commission, and on behalf of the Indiana Utility Regulatory Commission, Illinois Commerce Commission, Public Utilities Commission of Ohio, Kentucky Public Service Commission, Pennsylvania Public Utilities Commission, and West Virginia Public Service Commission (July 30, 2001); and Letter to Richard L. Miles from Hullihen Williams Moore, Commissioner, Virginia State Corporation Commission

process that the Alliance Companies developed and posted (without input from any stakeholders) was inherently flawed because the fundamental purpose of the stakeholder advisory process – to advise the independent board – could not be met because the Alliance Companies had failed to establish an independent board.<sup>5</sup> The position of the state commissions was further bolstered on August 2, 2001, when additional stakeholders, including three consumer advocate offices and several business and industrial customer groups, submitted a letter to the Commission’s ODR.<sup>6</sup> While the Commission’s ODR helped by promptly initiating an informal mediation, the ODR’s efforts have yet to result in the placement of an independent board.

Finally, on August 27, 2001, the Alliance Companies submitted their present filing. As part of the filing, the Alliance Companies set forth a plan to have National Grid serve as the managing member of the Alliance Transco and indicate that negotiations to develop and execute an LLC Agreement and related agreements in order to implement National Grid as the managing member are underway and will be filed with the Commission as soon as practical.<sup>7</sup> Previously, on May 15, 2001, National Grid had filed a petition for declaratory order seeking a determination that it would not be deemed a market participant with respect to the region served by the Alliance RTO and thus would be eligible to manage the Alliance RTO.<sup>8</sup> In an order issued on July 26, 2001, the Commission did not rule on the filing but permitted National Grid to supplement its petition in order to demonstrate how it satisfies the independence requirements of

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(July 31, 2001).

<sup>5</sup>The Alliance’s posted process would have had the stakeholders advise the Alliance *Bridgeco* until such time as an independent board is established.

<sup>6</sup> Letter to Richard L. Miles from Samuel C. Randazzo (Aug. 2, 2001) on behalf of Association of Businesses Advocating Tariff Equity; Coalition of Midwest Transmission Customers; Industrial Energy Users-Ohio; Missouri Office of the Public Counsel; Indiana office of Utility Consumer Counselor; Ohio Consumers’ Counsel, Illinois Industrial Energy Consumers; Citizens Action Coalition of Indiana, Inc.; Izaak Walton League of America, Inc., and Environmental Law & Policy Center.

<sup>7</sup> Alliance Companies August 27 Filing at page 5.

<sup>8</sup> See, *National Grid USA*, Docket No. EL01-80-000 (filed Aug. 27, 2001).

Order No. 2000.<sup>9</sup> Concurrently with the Alliance Companies' August 27 Filing, National Grid submitted the requested supplemental filing to establish that it is not a market participant and is therefore eligible to be the managing member of Alliance Transco. National Grid has also executed a Letter of Intent with eight of the ten Alliance Companies pursuant to which the parties have agreed to pursue the negotiation and documentation of definitive agreements to enable National Grid to make an investment in and serve as the managing member of the Alliance Transco. In their August 27<sup>th</sup> filing, the Alliance Companies, indicated that negotiations to develop and execute the LLC Agreement and related agreements are now underway and the parties expect to file a final agreement with the Commission as soon as practical.<sup>10</sup> The majority of the Alliance Companies also indicate that they fully support National Grid's request to be deemed a non-market participant.<sup>11</sup>

In addition to setting forth its plan to have National Grid serve as the managing member of the Alliance Transco, the Alliance Companies' August 27 filing proposes the establishment of an interim three-member board of trustees which would be authorized to make business decisions for the Alliance RTO until such time as National Grid is determined to be independent.<sup>12</sup> The Alliance Companies point to the uncertainty as to when the Commission might act on National Grid's petition as the primary reason for the establishment of an interim board of trustees.<sup>13</sup> According to the Alliance Companies' proposal, the interim board would have the responsibility to review and approve any actions proposed by the Alliance Companies respecting market design (as defined by the Alliance Companies) that may be necessary in order

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<sup>9</sup> *National Grid USA*, 96 FERC ¶ 61,121 (2001).

<sup>10</sup> Alliance Companies August 27 Filing at page 5.

<sup>11</sup> Alliance Companies August 27 Filing at page 4.

<sup>12</sup> Alliance Companies August 27 Filing at page 14.

<sup>13</sup> Alliance Companies August 27 Filing at page 14.

to meet the December 15, 2001 start date.<sup>14</sup> However, despite the Alliance Companies' assurances, the Alliance Companies' August 27 Filing seeks to impose limitations on the scope of functions for the interim independent board of trustees.

The Midwest State Commissions file these Comments in response to the Alliance Companies' August 27 Filing. The Midwest State Commissions respectfully request that the Alliance Companies proposed business plan be amended consistent with the recommended changes described herein.

## **II. DISCUSSION**

### **A. The Commission Should Reject the Proposed Limited Scope of Authority for the Interim Board of Trustees Because It Fails to Comply with the Commission's July 12 Alliance Order and with the Independence Requirement of Order No. 2000.**

The Alliance Companies' interim governance proposal, as outlined in its August 27<sup>th</sup> filing, does not meet the independence requirements of either Order No. 2000 or the Commission's July 12 Order. The Midwest State Commissions, therefore, request that the Commission reject the limited scope of authority for the interim decision-making entity in the governance proposal contained in the Alliance Companies August 27 filing and direct the Alliance Companies to adhere to the following: (1) compliance with the Commission's July 12 Order directives concerning interim independent decision-making; (2) impose consequences on the Alliance Companies for their failure to comply with the July 12 Order directives; and (3) direct the Alliance Companies to implement a permanent governance structure that comports with the independence requirements of Order No. 2000 and the Commission's July 12 Order as soon as possible.

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<sup>14</sup> Alliance Companies August 27 Filing at page 14.

The Commission initially established independence as one of the four characteristics required of an RTO, reaffirming its prior statements that “[a]n RTO needs to be independent in both reality and perception” in Order No. 2000.<sup>15</sup> Since Order No. 2000, it is well established that the Commission has held that “this principle should apply to all RTOs, whether they are ISOs, transcos or variants of the two.”<sup>16</sup> The importance of implementing a pre-RTO start-up independent decision-making structure that comports with independence requirements was further emphasized by the Commission in an order it issued simultaneously with its July 12 Alliance Order. In *GridSouth Transco, LLC, et al.*,<sup>17</sup> the Commission — in terms similar to those it expressed in the companion July 12 Alliance Order,<sup>18</sup> — expressed its concern about the lack of an independent board:

Although we previously accepted Applicants’ proposal on governance and independence, we are concerned that certain proposals that are central to independence, including the creation of an independent Board and a Stakeholder Advisory Committee, have not yet been implemented. *As a result, Applicants continue to make important policy decisions that will bind the RTO for the future.* We are mindful that Applicants are forging ahead to meet the December 15, 2001 start-up date. Yet, we are concerned that the GridSouth RTO is not currently independent of Applicants.

. . .

Accordingly, we direct that the independent GridSouth Board be seated in a timely manner. Moreover, *we direct the independent Board, and not Applicants*, to submit a revised compliance filing within 90 days.

*GridSouth*, 96 FERC ¶ 61,067 at 61,289 (emphasis supplied).

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<sup>15</sup> *Regional Transmission Organizations*, III FERC Stats. and Regs. ¶ 31,089 at 31,061 (1999), *order on reh’g*, Order No. 2000-A, III FERC Stats. and Regs. ¶ 31,092 (2000).

<sup>16</sup> *Id.*

<sup>17</sup> *GridSouth Transco, LLC, et al.*, 96 FERC ¶ 61,067 (2001) (“*GridSouth*”)

<sup>18</sup> 96 FERC ¶ 61,052 at 61,134-135.

The Commission also reaffirmed this principle in its July 12 Alliance Order, when the Commission made clear that it “remains committed to assuring the independence of RTOs from control by market participants.”<sup>19</sup> The Commission clearly articulated its concern that the Alliance Companies were making “business decisions prior to implementation of an Alliance RTO,” decisions that would potentially affect the future RTO’s ability to conduct its own operations.<sup>20</sup> To remedy the situation, the Commission ordered the Alliance Companies to take immediate steps to seat an independent Board to make such decisions. Specifically, the Commission stated:

Therefore, we direct Alliance Companies to decide which of the alternative business plans proposed they intend to implement within 45 days of the date of this order. *We further direct that from the date of this order an independent board be established to make all business decisions for the RTO.*<sup>21</sup>

Section V of the Alliance Companies’ August 27 filing<sup>22</sup> sets out the Alliance Companies’ belated proposal for decision-making independence during the interim period before the Alliance Transco is formed and before the Alliance RTO begins operations. The pre RTO startup independence proposal has two parts applicable to two different time periods. For the time period between the date that “the Commission determines that National Grid is a non-market participant” and the startup date of Alliance RTO operations, the Alliance Companies propose that “National Grid will assume responsibility for making all decisions for the Alliance RTO (subject to the Commission’s review authority) once its independence is established.”<sup>23</sup> For the period prior to the date that “the Commission determines that National Grid is a non-

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<sup>19</sup> 96 FERC ¶ 61,052 at 61,135.

<sup>20</sup> 96 FERC at 61,134.

<sup>21</sup> July 12 Alliance Order, 96 FERC at 61,134-135 (footnote omitted).

<sup>22</sup> August 27 Filing at 13 – 15.

<sup>23</sup> August 27 Filing at 14.

market participant,” the Alliance Companies propose to establish an interim three-member board of trustees. The Board of Trustees would remain in place “until such time as National Grid is determined to be independent.”<sup>24</sup> The interim board of trustees proposal specifically states:

Persons serving on the board would be individuals have [sic] no financial interest in a market participant and would have sufficient experience, expertise, professional stature and reputation that his or her selection as a board member of an entity of comparable assets and functions as the Alliance RTO would be appropriate. One board member would be selected by the Alliance Companies and one would be selected by the Alliance Advisory Committee. The third board member would be selected by the mutual agreement of the first two board members.<sup>25</sup>

The Midwest State Commissions do not find the proposed composition of the interim Board of Trustees or the proposed trustee selection process objectionable.<sup>26</sup> However, given the current timing, questions whether the interim board of trustees can reasonably be put in place and function in the short period of time that may exist before “the Commission determines that National Grid is a non-market participant” or, even, before the Alliance RTO begins operations. Regardless of the practicability of the proposal for interim trustees at this point in time, however, the restricted scope of functions that the Alliance Companies propose for the board of trustees is unacceptable and should, therefore, be rejected by the Commission.<sup>27</sup>

The Alliance Companies’ limitations on the proposed scope of functions for the board of trustees do not comport with the governance independence requirements prescribed by the Commission in Order 2000. The Alliance Companies propose to confine the Interim Trustees’

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<sup>24</sup> August 27 Filing at 14.

<sup>25</sup> August 27 Filing at 14.

<sup>26</sup> The ICC notes, however, that (1) currently, no Alliance Advisory Committee exists and that body would have to be constituted before it could make a trustee selection; and (2) the board composition and selection process should have been issued by the Alliance Companies on July 12 (or with the Alliance Companies’ compliance filing on January 16, 2001).

authority to “...review[ing] and approv[ing] any actions proposed by the Alliance Companies respecting market design (*i.e.*, long term congestion management, energy imbalance market and the ancillary services markets) that may be required to achieve a December 15, 2001 start date.” They also propose to limit the Interim Trustees’ scope of review and authority to act with regard to procurement of systems and adoption of operational practices necessary for initial (Day 1) operation of the Alliance Transco by requiring, among other things, the Interim Trustees to preserve the start-up arrangements already made by the Alliance Companies, absent clear and convincing evidence (to be evaluated by an unnamed person or persons) demonstrating that the arrangements are unduly discriminatory or preferential.<sup>28</sup>

The proposed limits on the Interim Trustees’ scope of functions ensures that the Interim Trustees would have no authority to review any prior or pending compliance filings made by the Alliance Companies or to amend the proposed Open Access Transmission Tariff. Further, the Interim Trustees would not have authority to review the implementation of the IRCA, an absolutely vital task in the promotion of seamless markets in the Midwest region. By asking the Commission to forego independent oversight of the Alliance Companies’ implementation of the IRCA, the Alliance Companies are unilaterally compromising the actions required to satisfy the seamless market objectives of the IRCA.

The Alliance Companies essentially ask the Commission to allow them to, in effect, start up the Alliance RTO themselves (despite their interest in the outcome as market participants) and present an interim proposal for so-called independent decision-making which does not permit true independent oversight over the initial practices and policies of the RTO that is slated

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<sup>27</sup> If the Commission does find National Grid to not be a market participant and National Grid steps into the role of interim decision-maker for the Alliance (prior to the operational start-up date for the Alliance RTO), the Commission must ensure that the scope of authority for National Grid is similarly not constrained.

to commence operation in a very short time. The Commission should not allow the independence provisions of Order No. 2000 to be circumvented to such a degree. It is vital that the scope of authority for the interim independent decision-maker not be improperly limited.

The Commission should require whatever independent board is seated (both interim, if seated, and permanent) to review and amend, as necessary, prior implementation decisions made by the Alliance Companies and the Alliance Bridgeco, going back to January 16, 2001 (or July 12, 2001, at the latest) as well as all future compliance filings. The Commission should be clear that neither the interim nor the permanent independent board need feel bound by any RTO development decision made by the Alliance Companies. Such review should be conducted in consultation with a Stakeholder Advisory Committee.<sup>29</sup>

Upon conclusion of such review by the permanent independent board, a thorough report should be issued and filed with the Commission. Costs arising from all Alliance Companies' RTO development decisions found to be imprudent by the Commission following review of the report should be disallowed for rate recovery purposes. The Alliance Companies should be advised by the Commission that they will bear the costs of all RTO development decisions ultimately rejected by the interim or permanent board, or found to be imprudent by the Commission. This recommendation properly puts the cost burden of improper RTO development decisions on the shareholders of the Alliance Companies - precisely where it belongs.

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<sup>28</sup> August 27 Letter at 14-15.

<sup>29</sup> The ICC presumes that any Stakeholder Advisory Committee that is developed will continue to advise the independent Board, or successor governing body of the Alliance RTO, even after the RTO commences operations. This is clearly called for under the Alliance Companies' own RTO proposal. *See* the Alliance Companies May 15, 2001 Supplemental Compliance Filing in Docket Nos. ER99-3144-004 and EC99-80-004, Attachment D (Section 6.6 of the Pro Forma Alliance Transco LLC Agreement) (Advisory Committee proposed to provide input and advice to the Managing Member).

The Midwest State Commissions support the formation of fully-functional RTOs that meet the requirements of Order No. 2000 and seeks the timely development of an appropriately formed RTO in the Midwest region. The Midwest State Commissions also support the Commission's July 12 directive ordering the Alliance Companies to immediately establish an independent board. The Alliance Companies failure to comply with the Commission's directives concerning interim independent decision-making and governance is unacceptable and must be immediately addressed. At a minimum, the Alliance Companies must bear the costs of decisions made by the Alliance Companies during the period in which an independent board should have been in place. Beyond this, the Commission should exercise its authority to penalize the Alliance Companies for not complying with Commission directives.

In short, the Midwest State Commissions firmly believe that the public interest is not served by allowing the Alliance Companies to put in place a compromised RTO with policies and procedures that were developed without the independent oversight that Order No. 2000 and the Commission's subsequent cases interpreting the independence characteristic require. The Alliance Companies proposal is designed to keep these and other important matters beyond the reach of their proposed Interim Trustees, thereby, preserving the Alliance Companies' ability to control key business decisions during the proposed service term of the Interim Trustees. The Alliance Companies' proposed Interim Trustees, if appointed, must have the same degree of authority and scope of functions as would an acceptable permanent independent governing board. Furthermore, the Alliance Companies, upon whom the Commission on July 12 placed the burden to immediately establish an interim independent decision-making board, must bear the consequences for not doing so.

The Midwest State Commissions, therefore, respectfully request that the Commission:

(1) reject the limited scope of authority for the trustees in the interim governance proposal contained in the Alliance Companies August 27 filing and (2) direct the Alliance Companies to comply with the Commission's July 12 Order directives concerning interim independent decision-making; (3) impose cost recovery and penalty consequences on the Alliance Companies for their failure to comply with the July 12 Order directives; and (4) direct the Alliance Companies to implement a permanent governance structure that comports with the independence requirements of Order No. 2000.

**B. The Alliance LLC Should Not be Required to Support the Alliance Companies' Cost Recovery for RTO Decisions Made during the absence of an Independent Board.**

A key provision of the National Grid – Alliance Term Sheet addresses the collapse of BridgeCo into the Alliance LLC. The provision in its entirety reads as follows:

On the Effective Date, Alliance LLC will acquire the assets, contractual obligations and other liabilities of BridgeCo for an amount in cash equal to the amounts contributed to BridgeCo by the Alliance Companies. Any loans from the Alliance Companies to BridgeCo will be assumed by Alliance LLC and repaid on the Effective Date. NGG and its affiliates will agree *to support recovery by Alliance LLC of all start-up costs and expenses*. To the extent the proceeds of any such contributions and loans were used by BridgeCo to fund start-up costs and expenses which are disallowed by FERC, (i) the Alliance Companies shall reimburse NGG or its designee the disallowed amount and (ii) an equitable adjustment will be made to the number of units held by NGG and its affiliates. Other than this assurance, the Alliance Companies will have no further obligations with respect to BridgeCo, and *Alliance LLC will defend, indemnify and hold harmless the Alliance Companies in respect of certain of such liabilities*, including those attributable to periods after the Effective Date. In the event that the Alliance Companies reimburse NGG or its designee for any disallowed costs or expenses as contemplated above, the amount that NGG is obligated to contribute to Alliance LLC under clauses (ii) and/or (iii) under "Capital Contributions by NGG" will be increased by a like amount.

The allocation of any such increase between clauses (ii) and/or (iii) will be determined based upon the nature of the disallowed cost or expense.<sup>30</sup>

The BridgeCo provision is objectionable to the Midwest State Commissions and must be modified by the Commission. The objectionable language in the provision commits National Grid and its affiliates to "support recovery by Alliance LLC of all start-up costs and expenses." It also requires Alliance LLC to "defend, indemnify and hold harmless the Alliance Companies in respect of certain of such liabilities, including those attributable to periods after the Effective Date." These provisions are not only unjust and unreasonable but also against the public interest. The Commission must ensure that the Alliance Companies bear the full risk of disallowance for all RTO development expenses they incurred, especially considering that they should have had an independent governing board in place as long ago as January 16, 2001 to make those decisions. Any proposal that binds National Grid to supporting cost recovery by Alliance Companies for costs of RTO development decisions made by the Alliance Companies during the period in which an independent board should have been in place to make such decisions clearly indicates the absence of the prerequisite independence between National Grid, the Alliance LLC and the Alliance Companies. The same rationale applies to the "indemnify and hold harmless" provision of the Bridgeco paragraph of the Term Sheet. Consequently, the Midwest State Commissions request that the Commission reject the term sheet provisions discussed herein. The Commission should order Alliance Companies to eliminate any provision from the term sheet which has the effect of hindering National Grid or Alliance LLC independence from the Alliance Companies or reducing the Alliance companies' cost recovery risk for RTO

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<sup>30</sup> National Grid – Alliance RTO Term Sheet at page 11-12 (emphasis added).

development expenses incurred during the period in which an independent decision-maker should have been in place.

**C. The Term Sheet Should be Amended to Include Alliance LLC “Call” Rights that Mirror the Alliance Companies’ “Put” Rights.**

Another key provision of the National Grid – Alliance Term Sheet that is related to an issue of concern for the Midwest State Commissions is the provision for Alliance Companies’ “put rights.” The pertinent language is found in the provision of the Term Sheet titled “Capital Contributions Following Transmission Service Date” and specifically provides as follows:

Alliance Companies will have the right to contribute Transmission Facilities to the Alliance LLC following the Transmission Service Date in exchange for units having a fair market value equal to the fair market value of the divested Transmission Facilities.<sup>31</sup>

These “put right” provisions, in and of themselves, are not objectionable to the Midwest State Commissions since exercising “put rights” is conducive to actual separation of transmission ownership from market participation. The Midwest State Commissions support that outcome under the proper circumstances. The ultimate goal of greater stand-alone transmission ownership/operation, however, could be further realized were the term sheet and resultant LLC Agreement to contain corresponding “call” rights for the Alliance LLC in addition to “put” rights for the Alliance Companies.

Indeed, the ICC previously made this recommendation for Alliance LLC “call” rights in its March 8, 2001 Comments on the Alliance Companies January 16 Order 2000 compliance filing. The ICC specifically commented:

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<sup>31</sup> *National Grid – Alliance RTO Term Sheet* at page 5 (A similar “put” right is described in the section of the National Grid—Alliance RTO Term Sheet titled “Put Right in Connection with IPO”).

One way for the Alliance RTO to become a transco is for member companies to divest their transmission facilities to the Alliance RTO. As it is, the Alliance RTO will merely exercise “functional control” over most of the facilities under its control and will not own those facilities and will not operate as a transco with respect to those facilities.<sup>32</sup>

The Midwest State Commissions’ position remains the same even under the new business plan proposed by the Alliance Companies in the August 27 Filing. Obtaining the positive features of the private for-profit transco form of RTO should not be entirely dependent on what is in the best interests of the Alliance Companies. Rather, the RTO design must take into consideration the public interest component. If the private for-profit transco form of RTO proves to be the superior model, as the Alliance Companies argue, then the public will have an interest in maximizing that result. The result of increasing the actual Transco features of the Alliance LLC, that is, increasing Alliance LLC transmission facilities ownership, can be advanced by providing the Alliance LLC with “call” rights on the transmission facilities of the Alliance Companies.

Such “call” rights would also further the objective of RTO open architecture that was required in Order 2000. The open architecture provision was included in Order 2000 to improve “the capability of the [RTO] to evolve in ways that would improve its efficiency.” Inclusion of a “call” right for the Alliance LLC would improve the efficiency of the Alliance RTO if the Alliance Companies are correct in their belief that the private for-profit form of RTO is superior to other forms.

The “functional control” to be exercised by the Alliance LLC over non-divested transmission facilities of the Alliance Companies will be little different from the functional

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<sup>32</sup> ICC Comments, *Alliance Companies*, Docket No. RT01-88-000, at 5 (March 8, 2001).

control that an independent system operator (“ISO”) would exercise over the transmission facilities of its members. If the private for-profit transco form of RTO is superior to the non-profit ISO form of RTO, its superiority primarily derives from its actual ownership of transmission facilities in combination with their operation independent of market interests. The superiority of the transco form of RTO, therefore, increases directly with the amount of transmission facilities it actually owns as compared to merely exercising functional control over. If the Commission agrees with the Alliance Companies that the private for-profit transco form of RTO is superior to the non-profit ISO form and that there are societal benefits available through separating both transmission operation and transmission ownership from market participant interests, then it follows directly that the Commission would want to advance that business form by providing the Alliance LLC with “call” rights over the transmission facilities of Alliance Companies.

**D. A Commission Ruling on The National Grid—Alliance RTO Term Sheet Provisions Concerning the Alliance Companies’ Proposal for an NDTO Advisory Committee Should be Held in Abeyance Pending the Commission’s Ruling on Section 6.6 of the Draft Agreement in the Alliance Companies’ Compliance Docket, RT01-88-006.**

The section of the National Grid—Alliance RTO Term Sheet titled “Advisory Committees” states as follows: “Alliance LLC will have the stakeholder advisory and NDTO [non-divesting transmission owner] advisory committees described in Section 6.6 of the Draft Agreement.”<sup>33</sup> The final provisions of Section 6.6 of the Draft Agreement are at issue in the Alliance Companies’ compliance docket, RT01-88-006, that was initiated with the Alliance Companies’ filing in that docket on August 31, 2001. To the extent that the NDTO provisions of Section 6.6 of the Draft Agreement are modified in Docket No. RT01-88-006, mirroring

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<sup>33</sup> *National Grid – Alliance RTO Term Sheet* at page 8.

modifications will need to be made to the National Grid—Alliance RTO Term Sheet. Accordingly, ruling on this provision of the National Grid—Alliance RTO Term Sheet should be held in abeyance by the Commission.

### **III. CONCLUSION**

**WHEREFORE**, for all the aforementioned reasons, the Midwest State Commissions respectfully request that the Commission: (1) reject the limited scope of authority for the trustees in the interim governance proposal contained in the Alliance Companies' August 27 Filing; (2) direct the Alliance Companies to comply with the Commission's July 12 Order directives concerning interim independent decision-making; (3) require the Alliance Companies to bear the consequences of their failure to previously comply with the Commission's independence requirements; (4) direct the Alliance Companies to implement a permanent governance structure that comports with the Commission's RTO independence requirements; (5) reject all provisions in the term sheet which might interfere with National Grid's or Alliance LLC's independence from the Alliance Companies; (6) require the term sheet be amended to include "call" rights for the Alliance LLC that mirror the Alliance Companies' "put" rights; and (7) defer ruling on any term sheet provisions involving a Non-Divesting Transmission Owner (NTDO) advisory committee until after the advisory committee issue is resolved in the Alliance Companies' separate compliance docket; and, for any and all other appropriate relief.

September 20, 2001

Respectfully submitted,

## **ILLINOIS COMMERCE COMMISSION**

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CERTIFICATE OF SERVICE

I hereby certify that I caused a copy of this pleading to be served this day upon each person designated on the official service list compiled by the Secretary in this proceeding, a copy of which is attached, in accordance with the requirements of Rule 2010 of the Commission's Rules of Practice and Procedure.

Dated at Chicago, Illinois, this 20th day of September, 2001.

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